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RUEATRS/DEPT OF TREASURY WASHDC
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RUCPDO/DEPT OF COMMERCE WASHINGTON DC
RUEHRC/USDA WASHINGTON DC
RUEHKO/AMEMBASSY TOKYO 1775
RUEHBJ/AMEMBASSY BEIJING 4897
RUEHBY/AMEMBASSY CANBERRA 2291
RUEHUL/AMEMBASSY SEOUL 4511
RUEAIIA/CIA WASHDC

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SIPDIS

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SENSITIVE

DEPT FOR EAP/MTS AND EB/IFD/OMA
TREASURY FOR IA-SETH SEARLS AND JWEEKS
SINGAPORE FOR SBAKER
TOKYO FOR MGREWE
COMMERCE FOR 4430/
DEPARTMENT PASS FEDERAL RESERVE SAN FRANCISCO FOR TCURRAN
DEPARTMENT PASS EXIM BANK
USDA/FAS/OA YOST, MILLER, JACKSON
USDA/FAS/OCRA CRIKER, HIGGISTON, RADLER
USDA/FAS/OGA CHAUDRY, DWYER

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SUBJECT: NEW BANK INDONESIA CHIEF FACES TOUGH ENVIRONMENT

REF: Jakarta 00355

11. (SBU) Summary: Parliament's Finance Commission overwhelmingly approved the appointment of Coordinating Minister for Economic Affairs Boediono to fill the post of Bank Indonesia (BI) Governor. Analysts expect Boediono to maintain the central bank's strong record of prudent monetary policy and independence from political interference. Boediono takes the reigns of the central bank in an increasingly difficult operating environment, as inflation surges, global economic conditions deteriorate, and the central bank faces corruption scandals. The appointment leaves a hole in the government's economic team and raises questions as to who will replace Boediono at the coordinating ministry. End Summary.

Boediono Approved as Central Bank Head

12. (U) Parliament's Finance Commission XI approved the appointment of Coordinating Minister for Economic Affairs Boediono as central bank governor by a 45 to 1 margin. Parliament had rejected the President's previous two candidates for the job, raising concerns about growing political tensions between the Parliament and the President (reftel). Parliamentarians praised Boediono's knowledge of monetary affairs and policymaking experience, citing his current role as Coordinating Minister for Economic Affairs and his previous post as Minister of Finance. Boediono also served as a senior official at BI during the 1990s.

13. (U) Analysts expect the new Governor to maintain BI's strong record of prudent monetary policy and independence from political interference. Observers also expect him to improve policy coordination on financial stability issues. Boediono's image as a clean and competent government official will help restore the central bank's image in the wake of graft allegations leveled against the current Governor and other senior officials this year. With post-graduate degrees from the University of Pennsylvania and Monash University in Australia, Boediono enjoys a solid reputation as a technocrat and reformer both at home and abroad.

Macroeconomic Pressures Mount

14. (SBU) Boediono takes the reigns of the central bank as inflation surges and global economic conditions deteriorate. Rising global food and oil prices have heightened concerns that BI may need to raise rates this year. CPI inflation now stands at 8.2% (YoY), above the 8.0% BI policy rate. Yet higher interest rates would dampen domestic demand at the same time sluggish global growth constrains expansion of Indonesia's exports. The uncertainty surrounding U.S. financial institutions and markets has increased risk aversion toward emerging markets such as Indonesia, even though Indonesia's banking system is relatively healthy with little exposure to U.S. subprime mortgages. Combined with lagging reform momentum in advance of the presidential and general elections in 2009, market analysts worry foreign and domestic investors may begin to retreat from Indonesia markets, putting downward pressure on the currency and reducing Boediono's ability to stimulate growth.

Boediono's Departure Leaves Hole in Economic Team

15. (SBU) Boediono's appointment ends speculation on who will run the central bank, but leaves a hole in the government's economic team. The role of Coordinating Minister for Economic Affairs is important to interagency policy coordination, a frequent problem in Indonesia, and to establishing overall economic policy. Recent press reports claim that the President is considering placing Vice President Jusuf Kalla in the vacant post, giving him a dual role in the government. While Kalla enjoys strong support in Parliament, analysts worry that the frequent policy disputes between Finance Minister Sri Mulyani Indrawati and Kalla will increase interagency acrimony and undermine economic policymaking. Analysts also consider Minister Mulyani, in a dual role as Finance and Coordinating Minister, and Raden Pardede, who parliament rejected for the BI Governorship, as frontrunners for

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the job. Other candidates for the position are largely businessmen-turned-politicians including Former Coordinating Minister for Economic Affairs Rizal Ramli, Ministry of Industry Official Fahmi Idris, Former Minister for Cooperatives and SMEs Adi Sasono, and Minister of Energy and Natural Resources Purnomo Yusgiantoro.

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